

## **MINUTES**

### **BOARD OF TRUSTEES OF THE PUBLIC EMPLOYEES' RETIREMENT FUND 143 West Market Street, Suite 500 Indianapolis, IN 46204**

**March 15, 2002**

#### Trustees Present

Jonathan Birge, Chair  
Richard Doermer, Vice Chair  
Teresa Ghilarducci  
Steven Miller  
Nancy Turner

#### Others Present

Mike Gery, Executive Assistant to the Governor  
Diana Hamilton, Special Liaison to the Governor for Public Finance  
Richard Boggs, Burnley Associates  
Stephanie Braming, William M. Mercer Investment Consulting  
Micah Fannin, William M. Mercer Investment Consulting  
Mary Beth Braitman, Ice Miller  
Eric Swank, Ice Miller  
Doug Todd, McCready & Keene, Inc.  
Karen Franklin, National City Bank  
E. William Butler, PERF Executive Director  
Patricia Gerrick, PERF Chief Investment Officer  
Tim Legesse, PERF Investment Analyst  
Joseph Duncan, PERF Investment Analyst  
Tommie Wilson, PERF Investment Assistant  
Krena Patel, PERF Intern  
Diann Clift, PERF MIS Director  
Ed Gohmann, PERF Legal Counsel  
Doug Mills, PERF Chief Financial Officer  
Jim Osborn, PERF Project Director  
Kevin Scott, PERF Director of Benefits Administration  
Kenneth Stoughton, PERF Director of Human Resources  
Lynda Duncan, Minute Writer

## ITEMS MAILED TO THE BOARD PRIOR TO MEETING

- A. Agenda of March 15, 2002 Meeting
- B. Minutes:
  - ❑ February 8, 2002 Board of Trustees Meeting
  - ❑ February 8, 2002 Benefits Administration Committee Meeting
  - ❑ January 16, 2002 Investment Committee Meeting
- C. Reports, Summaries, Memorandums and/or Letters Concerning:
  - ❑ Draft Request for Proposal for Actuarial Audit
  - ❑ Actuarial Valuations
  - ❑ Line-of-Duty Death Benefit Claims (3)
  - ❑ Member Service Reporting Charts
  - ❑ Year to Date Expenses Update

A quorum being present, the meeting was called to order.

## REGULAR SESSION

### 1. MINUTES APPROVAL

**MOTION** duly made and carried to approve the Minutes of the February 8, 2002 meeting of the Board of Trustees.

*Proposed by: Richard Doermer*

*Seconded by: Nancy Turner*

*Votes: 5 for, 0 against, 0 abstentions*

### 2. DISCLOSURES

Mr. Doermer – Bank One stock ownership.

### 3. EXECUTIVE DIRECTOR'S REPORT.

- Proxy Voting. Mr. Robert Beukema, Account Executive, and Mr. Robert Kellogg, Director of Policy, of the Institutional Shareholders Services (ISS) provided a presentation on their proxy voting and corporate governance services. ISS analyzes proxies and issues vote recommendations for more than 10,000 U.S. and 10,000 non-U.S. shareholder meetings each year. Ms. Ghilarducci noted that the purpose of proxy voting was to effectively employ shareholder rights attached to all equity. Under ERISA, there is a requirement to have a policy controlling how assets are voted because this entails the fiduciary use of assets. Although public funds are not necessarily bound by ERISA, the common understanding is that they are expected to conform to certain standards. The current policy is to defer to the fund managers to vote, although it was noted that this could sometimes result in a

split vote. Copies of the briefing were provided, which included information on the history of ISS, current developments in corporate governance and applications of policy. Additional issues were addressed, including how a fund such as PERF would establish a proxy-voting program that included the following broad areas:

- Recognition that proxy voting is a fundamental part of the overall obligation to manage the fund;
- Establishing clear guidelines and policies;
- Taking this to the members and employers;
- Basic fiduciary responsibility as outlined in ERISA.

Mr. Doermer asked how ISS formed its recommendations, and he was advised that percentage benchmarks are attributed using a binomial model involving a statistical computation. Mr. Birge noted that PERF owned stock in many companies and this raised a variety of issues. He was advised that ISS assessed issues on a case-by-case basis. There were common norms in the corporate governance world that are considered best practice.

Ms. Braitman noted the importance of making a decision early in equity investing on whether or not to infer fiduciary responsibility to the investment managers, as it is done at present, or to consolidate this responsibility with a proxy voting company. Ms. Ghilarducci noted that PERF had a responsibility to vote to the benefit of the members but the Board should be aware of the impact that a vote might have on environmental, social, economic issues in Indiana. Ms. Hamilton recalled that there was a provision for the Board to report on factors that might affect Indiana.

Mr. Doermer asked how recommendations were made on highly judgmental and subjective issues: social, economic and financial. He noted that most boards of directors were extremely conscientious when making such decisions. He asked what kind of voting power the firm had because their judgement in many of these areas could become very important. He noted that with the investment managers, the authority to vote was dispersed among many and he questioned if the shareholders were better off with that mix of judgement or having the voting power concentrated into a few hands.

Mr. Birge recommended referring this issue to the Investment Committee for further discussion and analysis.

- Internal Auditor. Mr. Butler distributed copies of the resume for Caroline Bradley, who will fill the new internal auditor position effective March 25, 2002.

**MOTION** duly made and carried to approve appointment of Ms. Caroline Bradley as the PERF Internal Auditor effective March 25, 2002.

*Proposed by:* Nancy Turner  
*Seconded by:* Richard Doerner  
*Votes:* 5 for, 0 against, 0 abstentions

- LEGISLATIVE REVIEW. Ms. Braitman of Ice Miller provided a summary of the legislation impacting on PERF's operations that had been approved by the Indiana General Assembly. In her remarks, Ms. Braitman noted that PERF had a most successful legislative session. She considered that these bills constituted some good legislation for PERF's members but acknowledged that this might involve additional work to implement the changes.

- ❑ HB 1004. Tax rates and credits; state spending cap. This Bill did not pass.
- ❑ HB1065. Annual PERF cost-of-living adjustment. This provides a cost of living adjustment in 2003 for members of PERF (or their survivors or beneficiaries) and for members of the State Teachers' Retirement Fund (TRF) (or their survivors or beneficiaries) who retired or were disabled before July 2, 2000. PERF has a 2% COLA built into its actuarial assumptions; TRF does not. There had been discussion of whether there would be any COLA that would affect both Funds and contingency measures had been planned to split the two separate COLAs. In the end, it was decided not to split the bill, and there is a single COLA that has provisions affecting both PERF and TRF. It is a one-year COLA and has been passed to the Governor for approval. Mr. Gohmann advised that PERF would receive a one-time COLA payable on January 1, 2003.
- ❑ HB 1081. Line of duty health care expenses for police officers and firefighters. This requires that a police or fire special service district, a town, a township, a fire protection district, or a provider unit in fire protection territories pay the medical and hospital care expenses for a police officer or firefighter who is injured or contracts an illness in the line of duty.
- ❑ HB1195. Tax and budget matters. This bill contains the Internal Revenue Code Update required to conform to Indiana's state tax laws to the version of the Internal Revenue Code as amended through January 1, 2002. This code was critical in preventing a disconnection between the 2001 changes in federal law and the state law provisions.
- ❑ HB1347. Public safety worker occupational disease or death. This creates a presumption that an emergency services employee or public safety employee who incurs death or disability from a health condition acquired while performing duties in the scope of the employee's employment and meets other requirements has incurred a death or disability in the line of duty and

provides for certain benefits. This presumption would be associated with an affidavit process stating that the person had not been exposed to these risks in other areas. This would represent a minimum extra administrative workload for the 1977 Fund.

- SB59. PERF and TRF administrative issues. This bill constitutes a significant administrative bill for PERF. It allows:
  - Pooling of assets of PERF and TRF for investment purposes. It authorizes PERF and TRF to enter into investment contracts for a term longer than five years.
  - It allows certain units in the 1977 police officers' and firefighters' pension and disability fund (1977 Fund) to buy back additional members' service.
  - It permits PERF and TRF to offer dental, vision, and long term care coverage to retirees. This is not mandated but provides a choice. Many cities and towns and employers have some kind of medical coverage available post separation, at least for a brief period. Mr. Osborn noted that there had been some discussion with union members who are very interested in this provision should the costs be more advantageous than those currently offered through COBRA. It was noted that the Texas Teachers' Fund had been mandated in their legislative session to form a health care pool. This would not constitute a profit-making option but would provide an additional incentive to customers. The Ohio Teachers' Fund is running a health care plan whereby they negotiate contracts with drug companies, prescription vendors, etc., in order to provide a retiree benefit program where they negotiate very low prescription drugs. It was considered that this option might be something for PERF to consider in the longer term.
  - It permits PERF and TRF members to purchase at actuarial cost additional service credit. For every five years of service, they could purchase an additional year. It allows the state or a political subdivision to pay all or a part of a member's contribution to purchase additional service credit.
  - It authorizes school corporations and political subdivisions to make payments to PERF and TRF using electronic funds transfers.
  - It provides for the creation of "rollover accounts" in PERF and TRF into which members can rollover certain money.

- SB60. Deferred Retirement Option Plan (DROP) for police officers and firefighters. It was noted that this was a popular bill for the police and firefighter community, although it implied additional administrative work for PERF's staff and will involve a substantial educational program. It gives members the ability, by declaring a retirement date in advance, to get a partial lump sum. Currently, their entire benefit is paid as a monthly benefit. The DROP program will expire in 2007, in time to coincide with expiration of the 50% Pension Relief Fund guarantee. On the city side, it allows the city to monitor when their officers will stop working and therefore provides better insight into retirement trends. Plans are already being made in conjunction with the 1977 Advisory Committee for PERF staff to explain to clerk-treasurers, pension secretaries, pension boards and officer the DROP program in various locations throughout the state. This bill also makes certain changes to the "dies in the line-of-duty" definition for the police officer and firefighter pension funds. The Pension Management Oversight Commission (PMOC) had proposed this change.
  - SB173. State police disability pension. It was notice that the State Police Department also intends to implement a DROP program as well as making some line-of-duty benefit changes.
  - SB269. PERF vesting for county elected officials. This provides that a person serving as a county clerk, auditor, recorder, treasurer, sheriff, or coroner is vested in PERF after: (1) either eight years of service in that office; or (2) ten years of service based on a combination of service as an elected county official and as a fulltime employee in another covered position. The number of people affected by this was estimated to be minimal.
  - SB374. Coalition to support Indiana seniors. This creates a coalition to support Indiana seniors and provides that membership in the coalition is granted to businesses that create a process that provides for an alternative payment date on which senior citizens may pay bills that are in conflict with Social Security, pension, or other retirement benefits.
- Contact Center Project. Ms. Cliff distributed a timeline setting out the anticipated progression of events. The Call Center supervisor had been hired and will join PERF on March 25. The Automatic Call Distribution software has been ordered and configured and a training program is being formulated. The projected start-up date is May 15, although training will be an on-going activity. Patrick Lane was asked what qualifications were required for the Contact Center Manager. He advised that the candidate was required to have the ability to interpret the accompanying software in order to measure call in-flows, types of call, types of members). The Manager should have the ability to manage and train his personnel, react to crises, and interpret the new IT system and how this will enhance customer services.

➤ Economic Growth and Tax Relief Reconciliation Act (EGTRRA). This Act contains a number of important retirement savings and pension reform provisions. Ms. Braitman provided an Executive Summary. Portions affecting PERF include:

- ❑ Changes in Contribution and Compensation Limits. The limits have been increased.
- ❑ Enhanced Portability among Plans. There is increased portability between retirement plans. These new rollover rules apply for distributions after 2001, and the new rules are mandatory for distributions from retirement plans. PERF is required to offer new opportunities for rollovers from PERF for retiring or terminating members. New administrative forms and notices and work processes have been created to make those changes. SB59 allows PERF to accept 403(b), IRA and 457 governmental plan rollovers.
- ❑ SB59 also adds a new rollover account to the Legislators Defined Contribution Plan.
- ❑ Permits PERF to accept rollovers from all permissible retirement savings vehicles (IRAs, 457 plans, 403(b) plans and other qualified plans). Rollover accounts could be invested in alternative funds, but SB59 does not allow the rollover account to be invested in the Guaranteed Fund.
- ❑ Surviving spouses now have all the rollover options, as well.
- ❑ SB59 allows all of the existing service purchases (military, etc.) to be made via a rollover. It provides for vastly expanded service purchase. One year of service may be purchased for every five years. It is an effective tool to buy up a higher level of benefit in a very tax effective way. Members can buy this service with pre-tax dollars. There are some rollover rules that staff is diligently working on and the various accompanying educational pieces.
- ❑ The new federal law allows deemed IRAs under employer plans. Effective for years after 2002, the Act provides that employers may permit employees to make voluntary contributions to deemed traditional IRA accounts and deemed Roth IRA accounts under “qualified employer plans”. In order to take advantage of the deemed IRA provision, an employer would have to amend its plan to allow participants to designate contributions as IRA contributions. It was noted that PERF should consider whether it wishes to suggest to PMOC that PERF should be allowed to establish deemed IRAs.

Ms Ghilarducci noted that pensions proposals recently passed by a United States House Committee had provided for a facility to buy investment advice with pre-tax dollars. She considered that this would benefit PERF’s customers by offering a complete package providing information on investment options and education. The importance of educating PERF’s clients as to their

retirement investment options was stressed it was suggested that this might be facilitated by producing a small investment information pamphlet.

- Actuarial Audit. A draft of the Request for Proposal (RFP) for the Actuarial Audit was included with the Board Meeting books. This focussed specifically on the 2001 actuarial valuation and a number of points concerning the actuarial service to be provided. The major points in the audit would be to review the validity of the data used by the present actuary and to provide a complete assessment of methods and procedures and adherence to standards. Mr. Butler asked for the timeline to be shortened. Following the Board's approval, the RFP would be published the following week, allowing a month for responses to be submitted by the May 10 Board Meeting, and to come back with a recommendation. The intention is to have the contract in place by early June and the work completed by September 1. This would be followed by the investment asset allocation study. The assignment would take 90 days. This is now standard practice for all medium and large pension funds. The RFP will include a caveat that any firm that is awarded the contract will not be eligible for actuarial work with PERF for three years.

**MOTION** duly made and carried to pursue the Request for Proposal for the Actuarial Audit.

*Proposed by: Teresa Ghilarducci*  
*Seconded by: Steven Miller*  
*Votes: 5 for, 0 against, 0 abstentions*

- Actuarial Valuations. Mr. Todd provided a summary of the results of the following actuarial valuations, as of January 1, 2001, covering a four year period, as follows:

- Police Officers' and Firefighters Pension and Disability Fund. The cost as a percentage of payroll is 23.6%, although they continue to recommend 21% which is considered to be on the conservative side. The figures display four years of results. In 1998, the Fund was over-funded by \$92 million. In 1999, they were overfunded by \$430,000. SB120 in 1998 resulted when converted retirees moved into the 1977 Plan. The return on the assets (actuarial) was 6% and the return on the assets (market) was -0.3%.

Mr. Doermer asked if McCready and Keene were considering any modification to the assumptions in light of performance of markets over the last 2 years. Mr. Todd advised that they had considered their interest rates to be on the low side but since March 2000 they had been comfortable with where the investment assumptions had been calculated. With the 'baby boomers' coming up and becoming more conservative, earnings were going to be more difficult.

- Excise Police and Conservation Officers' Retirement Plan. There had been a slight increase in cost as a percentage of pay roll. Last year the estimated salary



increases were 3.6% and this year they rose to 14.6% which has resulted in an increase in assumption percentage. The rise in salaries was attributed to their salary scales that are stepped based on service that resulted in actual salaries being ahead of the assumption. This was the reason for the increase in their employer contribution rate jumped from 15.7% to 17.0%

- PERF. The following contributions were established as of July 1, 2001: The contribution rate for the State increased from 5% to 5.2% attributable to the negative return in the Trust Assets. Because of PERF's policy of smoothing assets, which defers some of the losses, the impact this year was minor. The turnover assumption increased because more are terminating. Market value versus actuarial value last year and this year has changed and the future looks a little bleak. The wage freeze benefits the employer by reducing the employer contribution rates, which has resulted in a \$900 Million dollar saving with regard to the actual market value. The funded ratio has changed from 1.074 to 1.05%.

State contribution. The payroll is \$1.4 billion. If the old assumptions were used the State's contributions would have been 5.4%. For the assumptions, 5.2% is the recommendation for the state assumptions. This has moved from 5.0%, which means an extra \$3 million.

**MOTION** duly made and carried to approve the valuations for the Police Excise, PERF and the Police and Fire Fund.

*Proposed by:* Nancy Turner  
*Seconded by:* Steven Miller  
*Votes:* 5 for, 0 against, 0 abstentions

#### 4. INFORMATION TECHNOLOGY UPDATE

- Backfile Project. A total of 7.5 million documents have been converted. Reports on the project are being prepared and quality assurance procedures will be completed by April 1, 2002.
- SIRIS II Rollout. This may be delayed until April 20, 2002 in order to minimize problems on implementation. It is important to ensure that there are no conversion problems with data that might affect the accuracy of the payroll runs. There are four stages to the SIRIS project. They were using half of the system right now and the other half would come on line within the next 30 days. This will provide more effective tools to manage the data but will not constitute a 'magic fix'. The third stage will provide a remote dial in service and the fourth stage will provide the staff with a facility for report writing. These stages can be implemented within 30 – 45 days.
- Data Cleanup Project. Final comments have been received and it is anticipated that a new contract would be signed shortly. Work should

commence within 30 days. Navigant should have entered the missing data in the system within one year. The missing data retrieved by Navigant is verified and then keyed into the system on a regular basis.

- This will be an on-going process and data will continue to be reviewed and service credit verified.

## 5. LEGAL ISSUES.

- Disability Determination. Mr. Gohmann advised that since the last Board Meeting, a decision had been made against PERF on a case filed in 1996 concerning a disability determination. He had contacted the Attorney for the City of Plymouth, and the City had proposed that if PERF would provide the City with a list of procedures involved in disability determinations, the City would withdraw its appeal of the disability determination. Their local Board had decided that this was non-duty-related case but PERF had subsequently changed this determination without notifying the Plymouth authorities.
- Indiana Civil Rights Commission Complaint. A complaint had been filed based on an ADA issue. A firefighter was denied admission to the 1977 Fund because he did not meet the statewide baseline standards that had been adopted. His disability was not accommodated by the city that had given him a conditional offer of employment. He was bringing a complaint against PERF for denial of that membership.

## 6. 1977 FUND ADVISORY COMMITTEE.

- The 1977 Fund Advisory Committee had met on January 24, when the following issue was discussed:
  - ❑ Duty-related Disability Determinations. The Committee had made its first determination, when it had been decided that the disability was not duty-related. Under the new procedure, the local board sends its findings to the 1977 Advisory Committee, which makes a determination of whether or not the disability is duty-related. PERF issues a determination letter to the local pension board. This determination is subject to appeal. The Committee will be responsible for such determinations for all police officers and firefighters that have been determined as disabled after July 1, 2000. PERF will be responsible for administering the determination and processing any appeals.
- The 1977 Fund Advisory Committee had met on February 28, 2002 when the following issues were discussed:
  - ❑ Deferred Retirement Option Plan (DROP). Planning for regional seminars to communicate to all members of the 1977 Fund (clients, members,

employers and pension secretaries) details of the Deferred Retirement Option Plan had commenced. This option had generated considerable interest among the 1977 Fund's membership and represented a major communication initiative for PERF's staff. The DROP will come into effect on January 1, 2003.

- Line-of-Duty Death Determinations. The Board reviewed three Line-of-Duty Death Claims.

- **MOTION** duly made and carried to approve line-of-duty death benefit award in the case of Mr. Jerry A. Fisher, Deputy, Gibson County Sheriff's Department.

*Proposed by:* Nancy Turner  
*Seconded by:* Richard Doermer  
*Votes:* 5 for, 0 against, 0 abstentions

- **MOTION** duly made and carried to approve the line-of-duty death award in the case of Mr. Louis W. Donald, Officer, City of Gary Police Department.

*Proposed by:* Steven Miller  
*Seconded by:* Richard Doermer  
*Votes:* 5 for, 0 against, 0 abstentions

- **MOTION** duly made and carried to approve the line-of-duty death award in the case of Mr. Jerold J. Wyss, Officer, City of Decatur Police Department.

*Proposed by:* Steven Miller  
*Seconded by:* Nancy Turner  
*Votes:* 5 for, 0 against, 0 abstentions

Some discussion ensued on the difficulties involved in making such determinations. It was anticipated that new language involving L-O-D death claims incorporated in SB60 would provide additional guidance.

7. BENEFITS ADMINISTRATION COMMITTEE MEETING. Ms. Turner advised that the Committee had met that morning. Mr. Scott had provided a progress report on member service reporting for processing of refunds, retirements and new membership applications. Backlogs were being reduced. PERF could process incoming new records much faster due the additional support provided by temporary staff and the addition of a second scanner. The inventory backlog was being reduced by between 300-400 per month, and it is the aim to reduce this to zero. Mr. Doermer asked if the temporary employees were responsible for calculating refunds and disability payments. He was advised that this required a simple audit process.

8. INVESTMENTS. Steven Miller provided a summary of the Investments Committee Meeting held that morning:

- Round Table Meeting. A Round Table meeting will be held on March 22. Mr. Miller had asked for the subject of private equity venture capital investing to be included in the agenda. The Vice President of the Investment and Value Foundation had proposed a resolution to be handed out at the meeting. This essentially supported the initiative of making funds available for prudent investments in Indiana-based enterprises and business start-ups.
- Life Science Initiative. A Steering Committee, comprising members from Purdue and IU and State Universities, had been established to study the issue of bringing some of the products from basic research into commercial ventures for economic development. This involves ensuring that funds are available to support these initiatives when they come forward. A presentation on this initiative will be given at a future Board Meeting.
- Securities Lending. Ms. Gerrick had provided an update on Securities Lending.
- Small-Mid Search Update. The Small and Mid Cap Manager Searches, involving due diligence meetings, were in progress. The finalists will be interviewed at the end of March. Ms. Ghilarducci noted that it was important to be aware of the need for minority managers and advocated that representatives from this group should be amongst the candidates. She was advised that this was the case.
- Future Projects. This includes:
  - ❑ Actuarial Audit (May/June start)
  - ❑ Asset Liability Study (Fall 2002)
  - ❑ Concentrated value/growth equity search
  - ❑ Global search
  - ❑ Review of Index Fund providers and consolidation
  - ❑ Fixed Income Strategy

9. FINANCIAL. Mr. Birge advised that the final updated financial budget for 2002 was not complete for the full year with regard to some of the contracts and numbers.

10. EXECUTIVE SESSION

The Board met in Executive Session under IC 5-14-1.5-6.1(b)(9) (personnel evaluation) and 5-14-1.5-6.1(b)(2) (strategy with respect to litigation).

11. NEXT MEETING. The next meeting of the Board will be held on Friday, April 12, 2002, at 1:00 p.m.
12. ADJOURNMENT. There being no further business, the meeting was adjourned.